California Fair Political Practices Commission

MEMORANDUM

To: Chairman Getman and Commissioners Downey, Knox, Scott and Swanson

From: Holly B. Armstrong, Commission Staff Counsel
John W. Wallace, Assistant General Counsel
Luisa Menchaca, General Counsel

Re: Proposition 34 Regulations: Personal Loans (§ 85307) - Adoption of Proposed Regulation 18530.8

Date: December 27, 2001

Introduction and Background

Government Code § 85307[1], which was enacted by Proposition 34, provides:

> "(a) The provisions of this article regarding loans apply to extensions of credit, but do not apply to loans made to a candidate by a commercial lending institution in the lender's regular course of business on terms available to members of the general public for which the candidate is personally liable.
>
> "(b) A candidate for elective state office may not personally loan to his or her campaign an amount, the outstanding balance of which exceeds one hundred thousand dollars ($100,000). A candidate may not charge interest on any loan he or she made to his or her campaign."

At its meeting on November 5, 2001,[2] this regulation came before the Commission for its second pre-notice discussion. The regulation has now been noticed in its current form and may be adopted.[3] In that context, the Commission considered three issues: (1) whether personal loans made prior to January 1, 2001, the effective date of Proposition 34 and of section 85307, count toward the $100,000 loan limit imposed by section 85307(b), (2) the scope of the term "campaign" in the context of section 85307(b), and (3) whether a loan obtained by a candidate from a commercial lending institution, for which the candidate is personally liable, which the candidate then lends to his or her campaign counts toward the $100,000 personal loan limit imposed by section 85307(b).

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[1] All further statutory references are to the Government Code, unless otherwise specified.
[2] This regulation was presented for its first pre-notice discussion at the September 10, 2001, Commission meeting.
[3] Changes from the noticed version in subdivisions (b) and (c) are shown in strikeout and bold.

The Commission decided that personal loans made prior to January 1, 2001, do not count toward the section 85307(b) $100,000 personal loan limit, and essentially defined the scope of the term "campaign" for purposes of section 85307. The issue of the applicability of section 85307(b) to bank loans made to a candidate then loaned by the candidate to the campaign still remains as a decision point for the Commission's consideration. In addition, staff has rewritten subdivision (b) of the regulation to more accurately convey the Commission's decision at the November 5, 2001, meeting regarding the meaning of the term "campaign." In the course of drafting this change to the regulation, a second decision point arose regarding the scope of that definition, which is addressed below in decision 1. Therefore, there are two decision points before the Commission in this regulation.

PROPOSED REGULATION 18530.8

This regulation addresses primarily subdivision (b) of section 85307, dealing with the $100,000 limit on a candidate's personal loans to his or her controlled committee.

Treatment of Pre-January 1, 2001, Personal Loans

> (a) Any personal loan made before January 1, 2001, by a candidate for elective state office does not count toward the $100,000 loan limit of subdivision (b) of Government Code section 85307.

The Commission decided this issue at its November 5, 2001, meeting, and no substantive decisions remain concerning the treatment of pre-January 1, 2001, personal loans under section 85307(b). Pursuant to proposed regulation 18530.8(a), personal loans made by a candidate to his or her campaign prior to January 1, 2001, do not count toward section 85307(b)'s $100,000 personal loan limit.

DECISION 1 – Proper Scope of Term "Campaign"

In **Decision 1,** the Commission is asked to decide whether the term "campaign" should be limited to the candidate's own controlled committees formed for the purpose of an elective state office, or whether it should also include all committees formed for the purpose of supporting the candidate's candidacy for elective state office.

> (b) For purposes of subdivision (b) of Government Code section 85307 and this regulation, "campaign" encompasses both the primary and general elections or special and special runoff elections for a specific term of elective state office. "Campaign" includes any of the candidate's controlled committees formed for the purpose of seeking ~~an~~ **that** elective state office **{Decision**

> **1}**[and all committees formed for the purpose of supporting the candidate's candidacy for elective state office.]

In all likelihood, the committees formed for the purpose of supporting the candidate's candidacy to which the candidate might loan money, other than his or her own controlled committee, would be primarily formed committees.

> "'Primarily formed committee' means a committee pursuant to subdivision (a) of Section 82013 which is formed or exists primarily to support or oppose any of the following:
>
> "(a) A single candidate.
>
> "(b) A single measure.
>
> "(c) A group of specific candidates being voted upon in the same city, county or multicounty election.
>
> "(d) Two or more measures being voted upon in the same city, county, multicounty, or state election." (Section 82047.5)

As an argument against including the bracketed language, the candidate or candidates the primarily formed committee supports must not exercise any control over the activities of the committee, or else the committee becomes a "controlled committee" under section 82016. Section 82016 provides:

> "(a) 'Controlled committee' means a committee that is controlled directly or indirectly by a candidate or state measure proponent or that acts jointly with a candidate, controlled committee, or state measure proponent in connection with the making of expenditures. A candidate or state measure proponent controls a committee if he or she, his or her agent, or any other committee he or she controls has a significant influence on the actions or decisions of the committee."

"The Commission has interpreted the definition of 'controlled committee' very broadly to include any significant participation by a candidate, his or her agent, or representatives of any other committee he or she controls in the actions of a committee." (*Nerhus/Marler* Advice Letter, No. I-90-467.) This provides the argument in favor of including the bracketed language in the regulation, by raising the question of whether a candidate's making of a loan to a primarily formed committee constitutes significant participation in the actions of the committee, such that the primarily formed committee comes within the control of the candidate.

Staff Recommendation: Staff makes no recommendation on this point. However, staff sees no harm in including the bracketed language in the regulation.

DECISION 2 – Treatment Of Bank Loans Under Section 85307(b)

In November, the Commission wrestled over the two options presented by staff. The Commission was presented with what appeared to be a third option by an auditor from the Franchise Tax Board. He suggested that the candidate be permitted to borrow as much money as he or she wanted from the bank, but that any amount loaned to the campaign over $100,000 be contributed. The Commission directed staff to examine this third option further. Upon further discussion with the auditor and closer examination of the proposal, staff has determined that what, at first blush, appeared to be a third option was, in reality, a different way of expressing the existing option (a). Option (a) says that the proceeds of a bank loan apply to the $100,000 loan limit. The suggestion by the auditor also involved having the proceeds of the bank loan apply to the $100,000 personal loan limit, but would simply allow the candidate to also contribute the proceeds of a bank loan to his or her campaign, which raised additional issues related to reporting of expenditures by the candidate, but which were not related to and do not affect the issues presented by this proposed regulation.

What follows are the essential elements of the discussion presented in the memorandum dated October 25, 2001.

This decision point presents an issue of statutory construction for the Commission to consider that requires a review of the relevant underlying statutes.

Pursuant to section 82015(a):

> "'Contribution' means a *payment*, a forgiveness of a loan, a payment of a loan by a third party, or an enforceable promise to make a payment except to the extent that full and adequate consideration is received, unless it is clear from the surrounding circumstances that it is not made for political purposes." (emphasis added.)

"Payment," pursuant to section 82044, means "a payment, distribution, transfer, *loan*, advance, deposit, gift or other rendering of money, property services or anything else of value, whether tangible or intangible." (Emphasis added.)

Therefore, reading sections 82015 and 82044 together, a loan, which is a payment, is a contribution under the Act. For example, a loan from an individual that a candidate put into his personal bank account and later transferred to his campaign account was reportable and subject to the Proposition 73 contribution limits. (Perata, FPPC No. 2000/ 156.) Because a loan is a contribution, a loan would ordinarily be subject to the contribution limits set forth in sections 85301 and 85302.

However, section 84216 provides the following exception:

> "(a) Notwithstanding Section 82015, a loan received by a candidate or committee is a contribution unless the loan is received from a commercial lending institution in the ordinary course of business, or it is clear from the surrounding circumstances that it is not made for political purposes."

Accordingly, a loan to a candidate from a commercial lending institution is not a contribution.

A loan from a candidate's personal funds to his or her campaign, however, would still be a contribution to the campaign, but would not be subject to the contribution limits. Pursuant to section 85301(d):

> "The provisions of this section do not apply to a candidate's contributions of his or her personal funds to his or her own campaign."

Instead, with respect to personal loans, section 85307(b) imposes a limit of $100,000 on the outstanding balance of the loan that a candidate may make to his or her campaign.

Section 85307(a) provides that "[t]he provisions of this article regarding loans . . . do not apply to loans made to a candidate by a commercial lending institution in the lender's regular course of business on terms available to members of the general public for which the candidate is personally liable." Further, subdivision (a) contains no limiting language as to its applicability, whereas, subdivision (b) is limited in its application to candidates for elective state office. Given these issues as discussed below, the question then arises whether the $100,000 limit imposed by section 85307(b), applies to the proceeds of a bank loan made to a candidate and then loaned by the candidate to his or her committee.

Subdivision (c) provides the opposing options in **options a** and **b**, with **option a** providing that such proceeds *do* count toward the $100,000 personal loan limit imposed by section 85307(b), and **option b** providing that such proceeds *do not* count toward the $100,000 limit.

> (c) The proceeds of a loan made to a candidate by a commercial lending institution for which the candidate is personally liable, pursuant to the terms of subdivision (a) of Government Code section 85307, which the candidate then lends to his or her campaign **{Decision 2, option a/option b}** ~~[does/does not]~~ **[do/do not]** count toward the $100,000 personal loan limit imposed by subdivision (b) of Government Code section 85307.

Argument in Support of Option A

The strongest argument in support of **option a** is that it appears to be consistent with the policy expressed in the Voter Information Guide, i.e. to level the playing field by maintaining the integrity of the $100,000 personal loan limit imposed by section 85307(b). "In statutory construction cases, our fundamental task is to ascertain the intent of the lawmakers so as to effectuate the purpose of the statute." *Estate of Griswold*, No. S087881, 2001 WL 694081, at *3 (Cal. Sup. Ct., June 21, 2001).

Pursuant to section 84216, a loan ***to a candidate*** from a commercial lending institution in the ordinary course of business is not a contribution to the candidate's campaign. Pursuant to section 85307(b), a loan ***from a candidate*** to his or her campaign is limited to an outstanding balance of $100,000 at any given time. Therefore, by analyzing the process as two separate transactions, it is possible to conclude that when a commercial lending institution makes a loan ***to a candidate***, the funds become an asset of the candidate in the first transaction. In the second transaction, the candidate converts the funds he or she received from the bank, and ***the candidate loans the funds to his or her campaign***, thus making the funds subject to section 85307(b).

Section 85307(a)'s exclusion of loans from a commercial lending institution from application of provisions regarding loans may refer to sections 85301 and 85302, which are the contribution limits provisions. Under ordinary circumstances, loans are contributions. However, a loan from a commercial lending institution for which the candidate is personally liable is an exception to that rule, and, pursuant to section 85307(a), the contribution limits do not apply to these loans.

Another argument in support of **option a** is that if the loan is not considered a contribution of a candidate's personal funds, the voluntary expenditure limits would never be lifted as long as a candidate used monies obtained through a bank loan. (Section 85402.)

Argument in Support of Option B

However, there are factors that must be examined that support adoption of **option b** rather than **option a**.

Section 85307(a) states:

> "The provisions of this article regarding loans . . . do not apply to loans made to a candidate by a commercial lending institution in the lender's regular course of business on terms available to members of the general public for which the candidate is personally liable."

The term "loan" is found nowhere else in Chapter 5, article 3 except in section 85307(b). Therefore, one cannot escape the fact that the reference in section 85307(a) must, at a minimum,

include section 85307(b) within its scope. This may lead to the simple conclusion that section 85307(b) cannot apply to loans obtained by a candidate from commercial lending institutions in the ordinary course of business.

As illustrated by the roadmap of statutes listed at the beginning of this section, a loan from a commercial lending institution to a candidate in the ordinary course of business is not a contribution. One must question, then, whether a loan from a commercial lending institution can be subject to any contribution limits. The $100,000 personal loan limit set forth in section 85307(b) is, essentially, a contribution limit set on a candidate's personal loan of funds to his or her own campaign. If a loan from a commercial lending institution to a candidate in the ordinary course of business is not a contribution, there may be no statutory authority within the Act for the Commission to impose limits on those funds even when the candidate uses those funds in his or her campaign.

As discussed above, under one reading of section 85307(a), section 85307(b) is inapplicable to loans to a candidate from a commercial lending institution. Also, pursuant to section 84216, a loan ***to a candidate*** from a commercial lending institution in the ordinary course of business is not a contribution to the candidate's campaign. Pursuant to section 85307(b), a loan ***from a candidate*** to his or her campaign is limited to an outstanding balance of $100,000 at any given time. However, by analyzing the process of a candidate taking a loan from a commercial lending institution and lending it to his or her campaign as ***one*** transaction instead of two separate transactions, as discussed under **option a**, the conclusion is that the funds are proceeds of a bank loan that are not subject to the limits imposed by section 85307(b).

Staff Recommendation: Staff makes no recommendation on this issue. Staff, however, believes that a determining factor is how the Commission views the loan transaction in light of the discussion above.

The purpose of subdivision (d) is to clarify that the balance of the personal loans to the candidate's campaign may not, at any one time, exceed $100,000, but that additional loans may be made at any time when the loan balance is below the $100,000 limit. This subdivision was added merely to clarify the variable nature of the concept of the "loan balance" subject to the limits of section 85307.

In November, one Commissioner asked that this subdivision specify that it applies to each of the applicable committees of a candidate. This is reflected in the language.